
R&D Tax Relief: What to look out for in Groups & Staff Costs

When helping companies claim R&D tax relief, we often see groups of companies that want to claim. There are some pitfalls to be wary of.

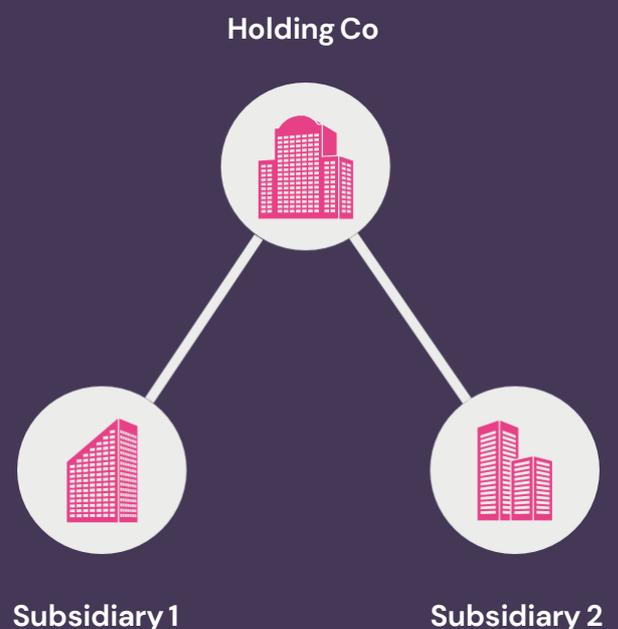
Our experience is that many undertaking R&D tax relief claims do not understand some of the rules and nuances that exist around groups.



What do we mean by a group?

If you're in a group, there's a good chance you already know it! However, for tax purposes, there are lots of different group definitions to access various tax reliefs. Here, we're talking about any inter dependency between companies.

A standard scenario would be a holding company with two subsidiaries (see diagram), but these pitfalls could apply to a range of different structures.



SME R&D Rules – An Overview

The SME R&D scheme is the more favourable of the two offered by the UK Government.

For this article, we will only be focusing on the SME scheme. To access it, having fewer than 500 staff members is the most important criterion. You'll also have to either have a turnover of less than €100 million or balance sheet net assets of under €86m.

Where a company carries out qualifying activities (i.e. undertaking a project to achieve an advance in science or technology) the company can claim R&D tax relief for qualifying expenditure, on those projects.

Expenditure that can qualify

The legislation is very restrictive and contains a list of expenditures that can qualify. Only revenue costs qualify, so capital costs cannot form part of a claim.

- **Staff costs**
- **Subcontractors**
- **Externally provided workers**
- **Consumables (including utilities)**
- **Software**
- **Data & cloud computing costs (from April 2023)**

Usually, most claims will include a significant amount of staff costs. This is where we find one of the largest and most common pitfalls.

Imagine a scenario where the holding company of a three-company group employs 200 staff members. There are four directors of the holding company, and they are all also directors of the two subsidiaries.

Contracts of employment are with the holding company and payroll is entirely run by the holding company. There are no payments made by either subsidiary for the staff.

Subsidiary One carries out R&D, and 50 of the staff members are involved, along with all four directors. The company wants to make an R&D claim, and the costs of their staff time (incurred in the holding company) spent on R&D is around £150,000.

The error we see time and again is that there should be no claim for staff costs for any of the employees (apart from potentially the directors). To be considered as 'Staff' requires a contract of employment with the claimant company. If all staff are employed by a separate company, there is no way to look through the group to another company and include the costs.

It is also important to underline that the holding company should not make an R&D claim if they are not themselves carrying out the R&D.

Externally Provided Workers

Where this claim could be saved, is under the 'externally provided workers' category of qualifying expenditure.

This allows a claim where workers are provided by a third party. This could be an unconnected and unrelated agency or the holding company (as per above). The normal rule for unconnected providers of workers is that you can claim 65% of the payment to the company. So, if we change our scenario to imagine one where an unconnected agency has provided our staff at a total cost of £200,000 (paid by Subsidiary One), then we could claim 65% of that: £135,000.

Where the parties are connected, the rules are slightly different, to stop artificially inflating a claim. In this scenario you can only claim the lower of the actual cost (i.e., the staff costs of the holding company) or the amount paid by the subsidiary. Where the subsidiary has made no payment, the claim amount is nil.

It is important when considering a new or large R&D project to ensure the structure you have in place supports your needs and the claim that you're making.



Directors

To be considered as an 'externally provided worker', you cannot also be a staff member of the claimant company. For directors, this can be difficult. HMRC's view is that a director is not eligible to be an externally provided worker. Therefore, even where there is a recharge of costs, if the director is not paid by the claimant company, their relevant costs may fall out of the claim.

There are some nuances; for example where payroll is run by one company as a matter of convenience, but the staff costs must "belong" to the claimant company, HMRC will expect to see the claimant company making payments for these resources..



How we can help

Easy R&D are specialists in not only submitting R&D claims to HMRC, but also in advising on some of the more complex points of the R&D eligibility rules. We have been advising on the SME R&D Tax Relief schemes since 2014, and have supported 1,000's of successful claims for groups and single companies.

If you're unsure or would like a no-obligation discussion to see if we can help, please do get in contact



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